Law Council
OF AUSTRALIA

Business Law Section

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To whom it may concern,

Submission on Amendments to the Family Trust Election Provisions

1. The Business Law Section of the Law Council of Australia (the **Committee**) urges Treasury to give immediate attention to the unintended and increasingly serious consequences of the Family Trust Elections (**FTEs**), Interposed Entity Elections (**IEEs**) and Family Trust Distributions Tax (**FTDT**) provisions in Schedule 2F to the *Income Tax Assessment Act 1936* (**ITAA 1936**).

2. As currently drafted and administered, these rules are creating real insolvency risks for taxpayers who have tried to comply with the law, including private groups that employ hundreds of Australians, and for the professional advisers who assisted them.

3. The Committee accepts, and does not seek to disturb, Parliament's legitimate objective of deterring loss trafficking and inappropriate franking credit streaming.

4. However, the FTDT regime is now operating in a way that goes far beyond that objective. It is imposing extraordinary liabilities, often with substantial accrued interest, in circumstances involving ordinary family and private group arrangements, historical administrative imperfections and no underlying tax avoidance mischief. Those outcomes are commercially destructive and cannot sensibly be regarded as the intended operation of the regime.

5. Although there is a strong case for more fundamental redesign, this submission proceeds on the basis that Treasury may prefer to retain the existing architecture of the FTDT regime and implement targeted legislative amendments to restore it to its original function. On that basis, the reforms proposed below are directed to a practical and urgent objective: preventing the regime from inflicting insolvency-level consequences on compliant taxpayers, significant private groups and their professional advisers where no abuse of the law has occurred.

6. If Treasury is open to broader structural reform, the Committee would welcome that discussion.

Background and overview of concerns with the current law

7. The Committee acknowledges the comprehensive submission to Treasury made by CPA Australia on 16 July 2025 'Submission on Amendments to the Family Trust Election provisions'. In this regard, Appendix B of CPA Australia's submission, provides useful background to this submission.

8. We also note the submission to Treasury by Chartered Accountants Australia dated 21 November 2025 'Family trust election and family trust distribution tax provisions Request for legislative amendments'.

9. The FTDT regime was enacted with effect from 9 May 1995 and introduced FTEs and IEEs as the mechanisms to define a "family group" and thereby limit the utilisation of losses incurred by non-fixed trusts (i.e. discretionary trusts) to the benefit of the family group with the economic control of that non-fixed trust. At that time, a new "special" tax, the FTDT was introduced, to be imposed at the top marginal rate plus Medicare levy on any distribution outside of the relevantly specified "family group", pursuant to the *Family Trust Distribution Tax (Primary Liability) Act 1998* (the **Act**).

10. It is clear from the Second Reading Speech and Explanatory Memorandum to the Act that the Government of the day did not plan for these rules to generate significant (or indeed, any) revenue for the Commonwealth—rather, as noted above, the FTDT regime was to act as a deterrent to entities that had made an FTE from distributing outside of their defined family group.

11. In his Second Reading Speech, the Hon. Christopher Miles MP went so far as to indicate that "*the government hopes the tax will never have to be paid*".[1] The Explanatory Memorandum to the Act notes that "*this tax need not ever be paid by any trust or interposed entity and in that sense is optional"*, and further that:

> *… there may be administrative costs on the ATO on the collection and recovery of the family trust distribution tax. However, the tax will only apply if trusts and relevant interposed entities fail to abide by the election they have made. It is hoped that the tax will never need to be collected.*[2]

12. Despite being enacted with effect from 1995, the FTDT regime attracted limited formal compliance activity by the Australian Taxation Office (**ATO**) for nearly three decades.

13. This approach appears to have changed materially in the second half of 2024, with significant ATO compliance activity and publications since that time.[3] This increased compliance activity has highlighted a number of technical deficiencies in the law that require urgent legislative reform, including:

    (a) **Amending an unlimited review period**: an FTDT liability can be identified 20 years after a distribution was made, with potentially crippling General Interest Charge (**GIC**)

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1 Commonwealth, Parliamentary Debates, House of Representatives (1 October 1997), 8936 (Christpher Miles).

2 Ibid [1.41].

3 See, eg, "Private Groups Stewardship Group key messages 19 November 2024", accessed on 28 April 2026; "Private Groups Stewardship Group key messages 24 July 2025", accessed 28 April 2026; "Spotlight on… Assistant Commissioner Amy James-Velagic", accessed on 28 April 2026; ATO webinar, "Family trust elections - What you need to know", 21 November 2024, accessed on 28 April 2026.

payable right back to the time of the original distribution without relief. This is particularly acute where records are incomplete or inconclusive;

(b) **Addressing the definition of family group**: the regime is poorly targeted, with FTDT liabilities arising inadvertently due to the precise and inflexible definition of a "family group" even where distributions have not left the economic family group, particularly as specified individuals pass away and family group dynamics evolve over time; and

(c) **Incorporating a discretion**: the lack of any discretion available to the Commissioner to forgive inadvertent omissions where the result under the Act is disproportionate to the technical transgression.

14. The issues currently giving rise to FTDT liabilities are largely of an administrative nature, including:

(a) the inability to locate physical elections;

(b) multiple elections made at different points in time without knowledge of earlier elections;

(c) no retention of physical elections by the ATO who now rely on potentially incomplete electronic records; or

(d) unawareness of the existence of earlier elections.

15. These issues are compounded by a number of systemic factors, including:

(a) a lack of reliable information on the status of historical elections, contributed to by the ATO's own poor record-keeping systems. The ATO's Online Services for Agents does not fully reflect all elections that have been made, and the reports available may show inconsistent or incomplete information on historical elections;

(b) taxpayers changing advisers and tax agents over the years, where the incoming adviser or tax agent was not aware of the prior election status. This difficulty is compounded by a lack of confidence in the accuracy of the ATO's FTE and IEE records, and the practical difficulty of obtaining reliable information about a client's election history when onboarding a new engagement; and

(c) the general requirement on taxpayers to retain records for five years, whereas FTDT matters can extend back indefinitely, making it unreasonable to expect taxpayers and their advisers to have retained the relevant documentation.

16. We consider there to be **three** key areas of reform that are essential to ensuring that the FTDT regime continues to operate as an effective deterrent to the specific mischiefs to which the law is directed, applying only in circumstances involving actual distributions outside of the economic family group. In addition, we recommend an interim moratorium on ATO compliance activity while a legislative solution is developed. These matters are addressed in turn below.

Priority One: Introduction of statutory time limit / assessment regime

17. The Committee recommends that the FTDT should have a formal assessment regime and a four-year amendment window, consistent with the period prescribed by section 170 of the ITAA 1936 for income tax assessments. The assessment regime and the amendment window may be subject to limitations for fraud, evasion, or deliberate loss trafficking arrangements. The introduction of such a limitation period would align the FTDT framework

with current legislative frameworks and the policy approach that applies across the broader income tax system, including in relation to other anti-avoidance provisions.

18. FTDT is not currently subject to a statutory period of review. Unlike income tax assessments, where section 170 of the ITAA 1936 confers finality on a taxpayer's affairs after two or four years, FTDT liabilities arise automatically at the time of a relevant distribution outside the family group, with no statutory or administrative time limit to when that liability may be identified or pursued. GIC is then payable at the full statutory rate right back to the time of the original distribution without relief.

19. The Treasury's *Report on Aspects of Income Tax Self-Assessment* published in August 2004 (the **ROSA Report**) noted in an income tax context that "*it is undesirable that a taxpayer who is not fraudulent or seeking to evade tax be exposed indefinitely to the possibility that their assessment will be increased to implement a particular provision"*. This led to Treasury explicitly recommending "*a detailed review of the specific provisions with unlimited periods to identify those that could have a set amendment period … [which] could be in line with the current general rules".*[4]

20. Having regard to the Commissioner of Taxation's (the **Commissioner**'s) sophisticated data-matching abilities, there appears to be no compelling reason for a period of review greater than four years in respect of FTDT liabilities. This time limit is now considered sufficient even for amendments under the general and specific anti-avoidance rules contained in Part IVA of the ITAA 1936.

21. For completeness we note that the ATO has indicated it considers itself unable to provide an administrative concession that would achieve the above result, and therefore a legislative solution is required.

Priority Two: Flexibility to make, amend and revoke FTEs and IEEs as circumstances change

22. There is a pressing need to provide more flexibility to taxpayers to make, amend and revoke elections where any benefits have only been conferred within the economic family group, or allow for retrospective elections to be made and any relevant FTDT paid. The current framework governing FTEs and IEEs is inflexible and does not adequately reflect the contemporary realities of family business structures and intergenerational transitions.

23. Currently, section 272-80 of Schedule 2F to the ITAA 1936 provides that an FTE cannot be varied or revoked except in extremely limited situations, and where arguably unnecessarily stringent requirements are met.

24. By way of example, none of the following circumstances would typically enable an FTE or IEE to be varied or revoked:

    (a) for any reason at all unless within 4 years of making the election (if seeking to revoke prospectively) or within 2 months after the end of an income year (if seeking to revoke retrospectively);

    (b) where the specified individual dies, and the family wish for the son or daughter of the specified individual to be the relevant reference point for the family group;

    (c) where a trust or company is sold at arm's length to a third party. In practice, there are numerous instances where shares in companies that have made an IEE have been

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[4] The Treasury, Report on Aspects of Income Tax Self Assessment (Report, August 2004) 34.

sold to unrelated third parties, and the incoming owner is burdened by a historical election it had no part in making;

(d) where companies have different classes of shares (Ordinary, A, B, C, etc) where the directors have a discretion to pay dividends and make capital distributions on one class of shares or another. This could arguably mean these companies may not satisfy the family control test in section 272-87 of Schedule 2F to the ITAA 1936, as the shareholders would not have fixed entitlements to the income or capital of the company, even where all classes are held by members of the relevant family group;

(e) where the wrong person has been specified as the specified individual due to an administrative error, but there is no underlying mischief as all benefits flow to the economic family group (as is the intention of the FTE/IEE regime);

(f) where an individual ceases to be part of the 'family' due to a relationship breakdown. For example, where a step-child of the specified individual is part of the family group by reason of the specified individual's relationship with the step-child's parent, the breakdown of that relationship may result in the step-child's spouse and children falling outside the family group, even though the step-child remains within it. This can trigger unexpected FTDT liabilities in circumstances where distributions have remained within the broader economic family unit;

(g) where a testamentary trust with independent trustees holds shares in a company that has made an IEE but is unable to make an FTE or IEE because it cannot satisfy the family control test in section 272-87 of Schedule 2F to the ITAA 1936. This situation commonly arises on the death of a key family member whose shares pass to a testamentary trust. The consequence is that the company cannot pay dividends without triggering FTDT, notwithstanding that the economic interest remains within the family; and

(h) where a testamentary trust with independent trustees holds shares in a company but is unable to make an FTE because it cannot satisfy the family control test in section 272-87 of Schedule 2F of the ITAA 1936. This situation commonly arises on the death of a key family member whose shares pass to a testamentary trust. The consequence is that the testamentary trust cannot pass on the franking credits to the beneficiaries.

25. In light of the above, the Committee believes that reforms are necessary to provide more flexibility to family trusts. These reforms will lead to more efficient administration of relevant trusts and decrease the burden of such cases on the ATO. These reforms should include, but may not be limited to, the following:

(a) additional revocation windows outside the current four-year window if the trustee can demonstrate that all distributions have remained within a family group throughout the period in which the election has been in force and no tax loss trafficking or franking credit streaming advantage has been accessed; and

(b) the ability to make retrospective elections to correct administrative errors, subject to payment of any FTDT attributable to distributions that genuinely flowed outside the family group.

26. To the extent any such changes are proposed to be implemented prospectively only, the Committee recommends a one-off opportunity to revoke or vary FTEs or IEEs as proposed in the Chartered Accountants Australia submission.

Priority Three: Introduction of Commissioner's discretion

27. The current legislative framework does not empower the Commissioner to exercise discretion with respect to the validity of FTE or IEEs. The Committee proposes that the Commissioner should have a statutory discretion to treat an election as valid, and to reduce the FTDT liability where there is an honest mistake or inadvertent omission, having regard to amounts that have been provided to members of the family group.

28. Currently, the Commissioner cannot disregard or waive FTDT where the taxpayer or adviser can demonstrate the liability arose from a mistake and no tax mischief has occurred. As noted above, the result under the Act can be disproportionate to the technical transgression.

29. Consideration should be given to a discretion broadly equivalent to the discretion in section 109RB of the ITAA 1936, which gives the Commissioner the discretion to disregard the operation of the deemed dividend provisions in Division 7A of the ITAA 1936 where a taxpayer has triggered those provisions through an honest mistake or inadvertent omission. Granting the Commissioner such discretion will preserve the deterrence of FTDT while removing the accrual of unlimited liability that produces outcomes contrary to Parliament's intention.

Interim measure: moratorium on ATO compliance activity

30. In addition to the above reforms, the Committee suggests a legislative moratorium on ATO compliance activity relating to FTDT as an interim measure while a long-term legislative solution is developed and implemented. The current position, in which the ATO continues to identify and pursue potentially significant FTDT liabilities while the law remains unreformed, risks compounding the very harm that the reforms outlined above are intended to address.

31. A moratorium of this kind is not without precedent. For example, in the context of payroll tax, the New South Wales Government legislated a 12-month pause on payroll tax audits of medical practices engaging general practitioners, during which period payroll tax that was payable but not paid was not subject to interest or penalty tax. A comparable approach to FTDT would provide breathing room for taxpayers and their advisers pending the enactment of appropriate reforms.

Further contact

32. The Committee would be pleased to discuss any aspect of this submission.

33. Please contact either Neil Brydges (Chair) [redacted] Tuan Van Lee [redacted] or Chris Atkinson [redacted] if you would like to do so.

Yours faithfully



Adrian Varasso
Chair
Business Law Section